

ANALYSIS OF AMENDED BILL

Franchise Tax Board

Author: Kuehl Analyst: Gloria McConnell Bill Number: AB 196
Related Bills: See Legislative History Telephone: 845-4336 Amended Date: 04-06-99
Attorney: Patrick Kusiak Sponsor: _____

SUBJECT: Child Support Enforcement/Establishes Department of Child Support/FTB
pilot Program for Current Support Obligations

SUMMARY OF BILL

This bill, as it directly affects Franchise Tax Board (FTB), would express the Legislature's intent to establish a one-year six-county pilot project to assess the benefits of referring to the FTB all child support obligations presently being enforced by the district attorney or local child support agency pursuant to the Welfare and Institutions Code.

The counties participating in the pilot would be selected by the Undersecretary of Child Support Services (Undersecretary), which is created by this bill. The selection would be by county application, in consultation with the FTB and local child support agencies. The referral of the obligations would begin by February 1, 2000, and end February 1, 2001. A report to the Legislature by FTB, with specified data, would be due February 15, 2001. The bill also specifies the criteria that would deem the pilot a success.

Additionally, certain persons currently required under federal law to file an information return reporting non-employee personal services (independent contractor registry [ICR]) for which \$600 or more was paid would be required to accelerate the reporting of those services and payments to Employment Development Department (EDD), operative July 1, 2000. The reporting would be required by the earlier of 20 days after entering into the personal service contract with aggregate payments in excess of \$600 or when payments made exceed \$600. The information could be used for child support enforcement, tax enforcement and EDD purposes.

This analysis will not address the remaining provisions in the bill, which all relate to child support enforcement.

SUMMARY OF AMENDMENT

The March 18, 1999, and April 6, 1999, amendments were to the child support enforcement provisions that do not directly affect FTB. The February 25, 1999, amendments added the above provisions that directly affect the FTB and certain of the child support enforcement provisions. FTB did not complete a previous analysis of this bill.

EFFECTIVE DATE

This bill would be effective January 1, 2000, with various operative dates. The Undersecretary would be appointed on or before January 1, 2000.

Board Position:

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_____ N	_____ OUA	_____ X PENDING

Department Director

Date

Gerald Goldberg

5/7/1999

The counties participating in FTB's pilot project would be selected and begin referring cases by February 1, 2000. The ICR reportings would begin July 1, 2000.

BOARD POSITION

Pending.

Each of the above provisions will be analyzed separately in this analysis. The FTB pilot project provision begins on page 2. The ICR provision begins on page 8.

FTB PILOT PROJECT PROVISION

LEGISLATIVE HISTORY

SB 240 (Speier; 1999) would establish a FTB pilot project to collect and enforce current support for Los Angeles County and establishes a Secretary of Statewide Child Support.

SB 542 (Burton; 1999) would establish a Department of Child Support Enforcement.

PROGRAM HISTORY/BACKGROUND

For purposes of this analysis, the following definitions are used:

"Arrearage" is the unpaid child support for past periods owed by a parent who is obligated to pay an amount for support by court order.

"Collection" means the receiving, receipt, and posting (cashiering) of money.

"Current support" is the amount of child support that meets the court-ordered support obligation for the current month.

"Delinquent," for purposes of FTB's delinquent child support enforcement program, is that amount that remains unpaid 91 days and more beyond the due date. However, for the statewide child support enforcement and collection program in general, may be used interchangeably with "arrearage."

"Due date" is the date specifically stated in the support order or, if no date specific is stated in the support order, the last day of the month in which the support payment is to be paid.

"Earnings (or wage) assignment" is an obligation ordered by the court requiring the employer to automatically deduct a fixed amount from the earnings of the obligor. Since 1994, all support orders must include an earnings assignment.

"Enforcement" is taking an action to compel payment of a child support or medical support obligation. An action involves both direct enforcement actions, such as seizure of a bank account, and indirect actions which result in payment of support, such as suspension of a business or driver's license.

Enforcement may include issuing wage assignments to employers for current support, a demand for payment of current, past due or delinquent amounts or levies to third-parties, including unemployment compensation, for delinquent support.

"Past due support," for purposes of FTB's delinquent child support enforcement program, is that amount that remains unpaid 30 to 90 days beyond the due date.

"Support order" means a judgment, decree or order issued by a court for the support and maintenance of a child, family and/or spouse. Support orders can include amounts for monetary support, health care, payment of arrearage, reimbursement of costs and fees and interest and penalties.

"Title IV-D" is reference to part of the federal Social Security Act that requires each state to create a program to locate noncustodial parents, establish paternity, establish and enforce child support obligations and collect and distribute support payments.

Title IV-D requires each state to have a plan that provides for a "single and separate organizational unit" to administer its child support plan. Under California law, the Department of Social Services (DSS), which is within Health and Human Services Agency, is designated California's single organizational unit to administer the state plan for securing child support, and its director is generally required to set forth the related policies (W&IC 11475). The county district attorneys (DAs) are delegated by law responsibility for establishment, enforcement and collection activities, which include the establishment of paternity (W&IC 11475.1) and securing a wage assignment by court order or other legal means (support orders). The DA may enforce a support order issued to any noncustodial parent for the benefit of any custodial parent, regardless of whether the custodial parent is or has been on welfare.

Beginning January 1, 1998, under California law, for those support orders that the DAs are responsible for enforcing, the DA:

- may voluntarily refer current child support obligations to FTB for issuance of a wage assignment and collection of the resulting payments.
- may voluntarily refer cases that are more than 30 but less than 91 days past due to FTB for enforcement as though they are delinquent final personal income taxes.
- is required, unless specifically excepted by DSS, to refer cases that are 91 days delinquent to FTB for enforcement as though they are delinquent final personal income taxes.

FTB receives from the DA only that information that is needed to enforce payment of the amount due, i.e., the identity of the obligor and the amount due. After FTB receives and collects payment, it notifies the Controller of the amount collected and to which referring county to transfer that amount. The DA maintains the case file information and distributes FTB child support collections accordingly.

The distribution is a complex process based on federal and state regulations. The county then disburses the moneys to the private party or governmental agency that has a claim on the funds. According to DSS, federal mandate phases in a "family first policy."

Child support delinquencies that accrue after the custodial parent received aid from the state and collected after October 1, 1997, will be distributed to the family first rather than to the state for reimbursement of the costs of that state aid. Beginning October 1, 2000, collections of child support delinquencies accrued before the custodial parent received aid from the state also will be distributed to the families first rather than to the state for reimbursement. In addition, regardless of when the delinquency accrues or is collected, the custodial parent may be eligible for the first \$50 collected, as an incentive payment. Therefore, while FTB knows the amount it collects, and in the case of multiple child support delinquencies for the same person, can provide basic accounting for the multiple collections, FTB does not know how the amounts are distributed and disbursed and what part was applied to the delinquency, if any. FTB relies on counties to provide updated balances on a timely basis.

The FTB, which is in the State and Consumer Services Agency, consists of the State Controller, the Director of Finance and the Chairman of the State Board of Equalization. The Franchise Tax Board administers the personal income, bank and corporation and related tax laws, which includes collection and enforcement thereof. FTB's peak season for processing tax returns is February through June each year. During FTB's 1998 peak season, FTB received and processed approximately 13 million tax returns and deposited \$13 billion in tax collections.

In addition to tax administration responsibilities, FTB collects and enforces payment of various non-tax debts as though they are delinquent final personal income taxes. One such debt is delinquent child support. Because FTB is authorized under existing law to collect and enforce current child support for counties on a voluntarily basis, FTB had begun to enhance its existing child support delinquency enforcement system to accommodate current support account processing. However, FTB did not receive sufficient interest from the counties to warrant continued enhancement of its existing system for this purpose.

FTB's delinquent child support enforcement program, which includes collection thereof, receives 66% of its departmental costs through federal reimbursement via DSS and the remaining 34% from the General Fund.

Under current tax law, FTB's child support enforcement activities must not interfere with FTB's responsibility to administer and enforce the Personal Income Tax Law (PITL). A collection priority is established under tax law whereby, if more than one debt is being enforced by FTB, FTB is required to apply amounts "being collected" first against personal income taxes and any remaining amount to child support.

To enforce payment of a debt, wages may be levied through either an assignment, a garnishment or a withholding order, primarily depending on the type of debt. A judgment creditor typically uses a wage garnishment for up to 25% of the debtor's disposable earnings per pay period. An earnings or wage assignment is typically used to enforce current child support. A withholding order is administratively generated, without court action. An administrative earnings withholding order for taxes (EWOT) is limited to 25% of disposable income. For child support delinquencies, an administrative withholding order issued by FTB is limited to 50% of disposable earnings, but for the DA, an administrative earnings assignment is limited to the greater of 3% of the arrearage or \$50. A support order can be modified to include in the wage assignment an amount for the arrearage.

In addition to traditional "earnings," a wage assignment or earnings withholding order for child support can attach amounts to become due an obligor on a continuous basis, i.e., rents, royalties and nonemployee compensation (contractual amounts).

When a delinquent child support case is referred to FTB, enforcement action includes the search for an employer and, if one is located, the issuance of an EWO. However, under current federal regulations, when an employer is located an earnings assignment for current support must be issued. Therefore, in order to meet federal regulations, the DA will frequently withdraw the case from FTB and issue the required earnings assignment for the amount of the current support plus 3% or \$50 (whichever is greater) to apply to the arrearage. Thus, replacing FTB's administrative EWO, which attached up to 50% of earnings, and resulting in lesser amounts collected. In order for a DA to increase the amount stated on the earnings assignment, the DA would need to return to court to modify the support order.

SPECIFIC FINDINGS

Currently, California's delinquent child support enforcement program is administered by FTB. DSS is the Title IV-D agency with the overall responsibility for California's child support enforcement program. The DAs remain responsible for maintaining the account information and case management. FTB staff responds to general questions regarding FTB's enforcement actions. In the event an obligor has questions about the computation of the amount due, the obligor is referred to the responsible DA.

Under this bill, the Department of Child Support Services (DCSS) would be created to replace DSS as the Title IV-D agency. An Undersecretary would be appointed to be responsible for overseeing and managing "the state's child support enforcement program" until the DCSS transitions into place, January 1, 2001.

Under this bill, it would be the intent of the Legislature to implement a pilot program to assess the benefits of referring to FTB all child support obligations for enforcement and collection of the amount due. For six "pilot" counties, FTB would be responsible for enforcement of current support and enforcement of amounts not delinquent or past-due. Upon application of the counties, the Undersecretary would select the six pilot counties and referral of the obligations would begin by February 1, 2000. The pilot period would be one-year, ending February 1, 2001. FTB's existing child support delinquency enforcement program would continue as required under existing law. FTB would be required to report on the pilot project to the Legislature by February 15, 2001. The pilot would be deemed a success if the amount of current child support collected by the FTB under the pilot project exceeds the amount of current child support collected by the respective pilot counties in prior years, adjusted by the average increase in collections in the pilot county for the past five years.

Under this bill, beginning March 1, 2001, the DAs' delegated child support enforcement responsibilities would shift to a new county department of child support services, to be implemented by all 58 counties June 30, 2002.

Policy Considerations

- Lines of authority for administering FTB's child support programs may be unclear since responsibility for administering the programs would be with the three-member FTB, placed under the State and Consumers Services Agency, but the Undersecretary would be required to manage the programs.
- In the event a personal income tax (PIT) tax debtor also owes current or past-due child support, FTB's enforcement priority is unclear. Currently enforcement of PIT takes priority over delinquent child support enforcement. However, federal regulations require that once an employer is located, an earnings assignment must be issued and take precedent over any other earnings assignment, withhold order and/or other levy.
- The workloads created by this bill could compete against FTB's core responsibilities and processes for PIT, especially during FTB's peak PIT filing season.

Implementation Considerations

Staff's initial concern is that the pilot project cannot be implemented by the FTB within the required time frames. From the date of enactment, it would take approximately 16 months to complete the feasibility study report (FSR) process and the programming and testing of the computer systems. If the bills were enacted this fall, 16 months places the processes and systems in place by early 2001; however, staff raises concern that implementing this new process during peak season could disrupt tax return processing. Staff, therefore, strongly suggests the pilot project begin implementation July 1, 2001.

Aside from the time frame concern, staff anticipates the pilot project could be implemented in either of two ways: (1) focus on the enforcement and collection workload generated solely by the pilot project; or (2) anticipate that the pilot project would be successful and create within the pilot project the ability for FTB to accommodate the workload for enforcement and collection of Title IV-D child support cases on a statewide basis. In either plan, FTB would continue expansion of its existing child support data base to incorporate current support cases and add the capability of issuing earnings assignments for current support cases to the automated enforcement system (Accounts Receivable Collection System [ARCS]), which is being designed with a targeted implementation date of June 2000. However, for the collection workload, the plans significantly differ because while FTB's existing collection computer system has the capacity to process the pilot project's estimated 1.3 million additional payments annually, it does not have the capacity to process the statewide estimated 10 million payments annually. If plan #1 (pilot plan) were implemented FTB would merely expand its existing tax collection computer system to accommodate the pilot project workload, but under plan #2 (statewide plan), a new collection computer system would be required.

To begin the programming and testing of the computer systems immediately following approval of the feasibility study report (FSR) process, staff further suggests that the bill provide an appropriation for fiscal year 2000/01, of which 66% would be paid from federal reimbursement received from DSS/DCSE and 34% from the General Fund.

Further, most pilot projects that FTB has implemented were for a duration longer than one year, which would be the period allowed under this bill. Staff has raised concern and is further exploring whether one year would be sufficient to measure the pilot project and whether sufficient data and statistics are available regarding the current systems to adequately measure the success of the project as detailed by the bill.

As suggested above, assuming a July 1, 2001, implementation date for referral of current support information and an appropriation for FTB's departmental costs, implementation of this bill for purposes of this analysis further assumes:

1. The six pilot counties would be the same as those in FTB's original pilot project for its child support delinquency program: Fresno, Los Angeles, Nevada, Santa Clara, Solano, and Ventura.
2. The counties would obtain or otherwise assure the existence of a support order and continue to perform case management on all child support accounts for which it is responsible. Rather than send FTB a copy of the support order, staff assumes the counties would transmit to FTB sufficient information (in a form and manner prescribed by FTB, as required by the bill) for it to issue or transfer the earnings assignment or otherwise enforce the support order, including employer information if known. It is also assumed the bill would clearly require the pilot counties to delegate to FTB the authority to enforce the support orders on the current support cases they are referring to FTB. It is also assumed, but the bill needs to clarify, that earnings assignments issued and in effect on a case prior to the referral date would continue to be in effect at the time of referral, but the case would be referred to FTB for monitoring of the earning assignment and enforcement as needed.
3. For the pilot period, which would begin July 1, 2001, FTB would receive from the six counties information on approximately 170,000 current support orders. FTB would collect per year approximately 1.3 million payments as a result of the pilot project. As a result of the support orders and/or earnings assignments referred under the pilot project, FTB would issue 800,000 notices (including enforcement notices).

Of additional concern, is that the Department of Information Technology and the Administration had a plan for a consolidated data center to occur after Y2K issues have been resolved. This consolidated data center plan could affect the implementation plan envisioned in this analysis.

FISCAL IMPACT

Departmental Costs

As the bill moves through the legislative process, the envisioned implementation plan may be revised and/or costs modified. However, under the above discussed implementation plans, staff preliminarily estimates that FTB departmental startup costs would range from \$13 million to \$28 million as follows for fiscal year 2000/01:

	Costs (in millions)	
	Plan 1 Pilot only	Plan 2 Statewide
Collection system	\$ 1.0	\$15.0
Enforcement data base	5.5	5.5
Automated enforcement system	5.3	5.3
Departmental overhead	.9	2.1
Total	\$12.7	\$27.9

This analysis does not take into account all of the following costs that have the potential of significantly increasing the costs identified in this analysis:

- facilities and related/associated costs,
- security,
- network and communications infrastructure, and
- main frame system capacity.

Collection Estimate

The data and information necessary to determine the collection impact of the one-year pilot program are not available. To the extent the department is able to receive child support payments earlier than the DAs as a result of this bill, there could be an acceleration of child support collections.

This estimate does not take into consideration the affect that this bill may have on competing debts, as discussed under Policy Consideration.

This estimate does not consider the possible changes in employment, personal income, or gross state product that could result from this bill.

INDEPENDENT CONTRACTOR REGISTRY PROVISION

LEGISLATIVE HISTORY

AB 780 (Caldron; 1999) requires state agencies to report independent contractors.

PROGRAM HISTORY/BACKGROUND

AB 573 (Kuehl; 1997), as amended May 15, 1997, would have created a independent contractor registry identical to the one to be created under this bill.

Employers are required to file employee quarterly wage reports to EDD. EDD's employer/employee information is available to FTB for delinquent child support enforcement and PIT enforcement shortly after the end of each quarter. In addition, employers are required to report their employee's name and SSN to EDD within 20 days of the hiring, rehiring or return to work of an employee (New Employee Registry (NER)) **SB 1423; Stats. 1992, Ch. 850**). The NER was enacted to help enforcement actions against those individuals able to avoid collection because the quarterly return information was received too late to be used as an effective enforcement resource. EDD may impose a penalty against employers that fail to report new employees as required.

Under the Personal Responsibility and Work Opportunity Reconciliation Act of 1996, by October 1, 1997, all states are required to operate a state directory of new employees, whereby all employers must report all new employees not later than 20 days after employment, or twice a month if reporting electronically. California's NER satisfies the federal mandate.

Under current law and practice, FTB uses an automated enforcement system to garnish wages and attach bank accounts of debtors. Typically, the automated enforcement system uses the debtor's SSN to search tax records and tax information returns filed by banks, other third parties, EDD records and 1099 information to locate the debtor's assets. Upon a match of the SSN and the asset, a withholding order is issued. An order to withhold (OTW) is issued for bank accounts, cash, and cash equivalents. Continuous OTWs generally are used to attach contractual payments and/or nonemployee compensation. Earnings withholding orders (EWO) are used to garnish wages or, in the case of child support enforcement, may attach contractual payments and/or nonemployee compensation. An EWO for delinquent child support generally attaches 50% of the payment due the obligor.

To use EDD's quarterly wage information, FTB accesses EDD's data base. However, for FTB to use EDD's NER, EDD requires that FTB provide a magnetic media tape containing a list of the delinquencies. For enforcement of child support delinquencies, FTB routinely provides EDD with its list. However, the voluminous size of the PIT file precludes FTB from using this process for PIT enforcement.

SPECIFIC FINDINGS

Under Section 6041A of the Internal Revenue Code (IRC), persons in a trade or business (service-recipients) that pay \$600 or more for personal services to an independent contractor are required to file an information return (1099MISC) with the IRS by February 28, following the close of the calendar year. The 1099MISC contains the following information:

- the name, address, and federal identification number of the person filing the information return,
- the name, address and identification number of the independent contractor (SSN in the case of an individual), and
- the aggregate amount of the payments made to that person.

For California purposes, service recipients are required to send a copy of their federal 1099MISC to FTB at the same time it is required to be filed with the IRS. If a service recipient has more than 250 independent contractors, the 1099MISC copy must be filed with FTB on magnetic media, which is generally available for FTB to access by May or June following the close of the calendar year. If the service recipient has fewer than 250 independent contractors, it may elect to file a combined federal/state 1099MISC or file a paper information return. In the case of a combined or paper information return, IRS shares the information contained on the information return with FTB, and this information is generally available for FTB access by November following the close of the calendar year.

Under this bill, service-recipients who are required to file an independent contractor information return under Section 6041A would report to EDD the same information required on the 1099MISC described above, plus the following additional information:

- the date of the contract or, if no contract, the date that payment first exceeded \$600, and
- the total dollar amount of the contract, if any, and the contract expiration date.

The information would be reported the earlier of 20 days after entering into the personal service contract or, if no contract, first paying more than \$600.

Implementation Considerations

FTB staff anticipates it would use the Independent Contractor Registry (ICR) for child support enforcement in the same form and manner that it uses EDD's NER. If the ICR information is matched with a delinquent child support obligor, FTB would issue a 50% wage withholding order on the nonemployee compensation.

Technical Consideration

Page 9, lines 23 and 24 references "paragraph (A) of subdivision (a) of Section 6041 of the Internal Revenue Code." The correct reference is "subdivision (a) of Section 6041A."

FISCAL IMPACT

Departmental Costs

Currently, EDD charges FTB for its use of the New-Employee Registry for child support purposes. Assuming the costs for the Independent Contractor Registry were approximately the same, the costs per fiscal year could be in the \$10,000 range and would be included in the child support enforcement program's annual budget.

Collection Estimate

Estimated Impact of AB 196 on FTB's Delinquent Child Support Enforcement Program Independent Contractor Registry Fiscal Year (In Millions)			
	2000-1	2001-2	2002-3
Independent Contractor/Delinquent Child Support	+\$1	+\$3	+\$5

This estimate does not consider the possible changes in employment, personal income, or gross state product that could result from this bill.

This estimate is based on the results of FTB's existing delinquent child support enforcement program and 1099MISC information available to FTB reported under IRC Section 6041A (non-employee compensation). In addition, the following data and assumptions were used:

- FTB would use the ICR for collecting delinquent child support in a manner similar to the NER and issue 50% earnings withholding orders.
- EDD would process the service-recipient information within 30 days of receipt in a format that FTB can use to match child support records submitted by FTB.
- By the third year, the maximum reporting compliance rate would be achieved, which would be two-thirds (22% the first year, 44% the second year).
- Adjustments were made in the first year to exclude pre-existing contracts and to allow for implementation lags.
- The average contract period is six months.
- The average collection amounts for independent contractors were based on the total child support collections through earnings withholding orders divided by total returns with reported salaries and wages, increased by 50% to reflect potentially larger incomes of independent contractors.

This estimate includes increased collections by FTB only for its existing delinquent child support program. This estimate does not take into consideration increased child support obligations for current support that would be collected by local child support agency or FTB's pilot program as a result of the reporting required by this bill.

This estimate assumes the ICR would be managed by EDD similarly to the NER, thereby precluding FTB's use of the registry for PIT collection purposes.